

**May 2018 saw a substantial slowdown in headline inflation - to 11.7% yoy.** The CPI was unchanged month-on-month.

A further decline in annual inflation had been expected, and the May reading came in somewhat below the NBU's projected inflation trajectory, which was published in the April 2018 Inflation Report. This was mainly the result of a sharp slowdown in food price inflation. In addition, administered prices grew less rapidly than in April, as the growth in tobacco prices decelerated and public utility tariffs increased at a more moderate pace.

As anticipated, the effects of the temporary supply factors that caused inflation to come above the NBU's forecast in H2 2017 and beginning of 2018 have been gradually fading. This was a result of the more favorable weather compared to last year's late frost, and more ample import supply. Another factor was tight monetary policy of the NBU. Its effect was the strongest in the exchange rate channel - the hryvnia exchange rate has been strengthening since late January 2018.

At the same time, further increase in production costs, wages in particular, and a rapid recovery in consumer demand, continued to put upward pressure on prices.

**Core inflation decelerated in May, to 9.3% yoy (stood at 0.2% mom).** In contrast to the previous two months, the annual rate of core inflation came in slightly lower than the NBU's projections.

In particular, the prices of services showed a much slower increase (by 14.3% yoy), inter alia, due to the strengthening of the hryvnia effective exchange rate. This dynamics was seen, in particular, in the costs of tourist and excursion services and domestic resort services (to 12.2% yoy and 3.4% yoy respectively). In addition, the growth in the housing maintenance costs continued to decelerate (to 37.2% yoy) due to the waning effect of a high comparison base, while slower growth in taxi fares (to 17.8% yoy) reflected a slight slowdown in annual price growth for fuels. The rise in the cost of a number of other services (such as personal care, mobile telecommunications, cable TV, healthcare advisory services, and dental care) accelerated, driven by robust consumer demand and growing production costs, including due to rising wages.

The growth in the prices of highly processed foods continued to slow (to 11.4% yoy). This was a result of a more moderate rise in the prices of raw materials, inter alia, due to a more ample import supply and the strengthening of the hryvnia against the currencies of Ukraine's trading partners.

Specifically, growth in prices for meat and dairy products continued to slow (to 20.0% yoy and 13.9% yoy respectively). At the same time, growth in clothing and footwear prices slightly accelerated (to 2.4% yoy), annual rate of increase in prices for other non-food prices remained flat compared to the previous month (at 5.0%), reflecting rising consumer demand.

**The growth in raw food prices slowed markedly (to 14.5% yoy),** coming below the NBU's forecast. The rate of growth in the prices for fruit and vegetables slowed significantly (to 2.4% yoy and 15.7% yoy, respectively). This was especially true for the prices for vegetables used in cooking borsch, and vegetables grown from seed, such as cucumbers, tomatoes, and eggplants (to 0.2% yoy and 16.6% yoy respectively), which were weighed down by more ample supply. The rising supply and a drop in global prices caused fruit prices to decline, particularly for bananas and citrus fruits (to 10.6% yoy and 4.9% yoy respectively).

The decline in global meat prices contributed to a slower growth in the prices for meat products in Ukraine (to 22.4% yoy). Raw milk prices also rose at a somewhat slower pace (16.6% yoy), following a similar trend for the purchase prices of raw milk, and the growth in exports of dairy products somewhat weakened. At the same time, egg prices rose faster (101.7% yoy), amid strong demand abroad.

Administered prices slowed (13.3% yoy), virtually in line with the NBU projections. Tobacco prices increased less quickly than in April (29.4% yoy). In addition, growth in utility prices moderated (to 4.5% yoy) due to a smaller increase in utility tariffs compared to last year. This outweighed the further acceleration in the growth of railway and air transportation costs (to 8.7% yoy and 12.2% yoy respectively) and the costs of urban public transport (to 21.9% yoy).

**The growth in fuel prices slowed (to 16.5% yoy)** as the hryvnia strengthened against the currencies of Ukraine's trading partners, especially the euro (the excise tax on fuels is set in the euro). However, these prices came in above the forecast, due to a steeper increase in global oil prices than expected.

**In May 2018, the PPI inflation accelerated to 16.5% yoy from 14.1% yoy in April.** Month on month, the producer price index rose by 0.8%.

Thus, in May, prices in the mining industry grew at a faster pace (18.9% yoy). In particular, prices in production of metal ores reversed from the previous month's decrease as the effect of a favorable base of comparison faded out (rose by

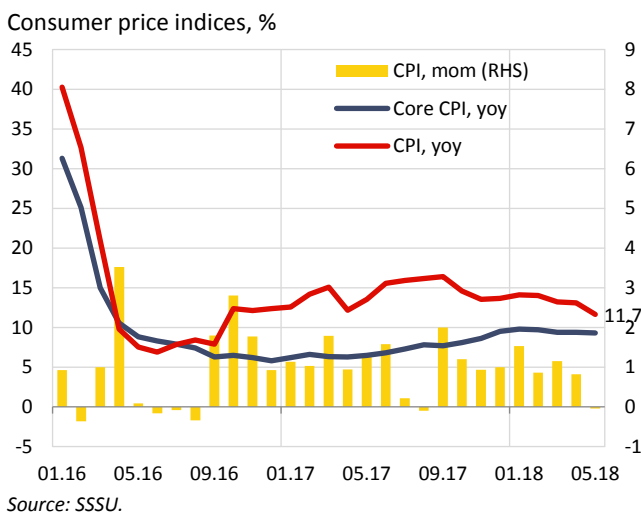
16.1% yoy compared with a decline of 2.6% yoy in April). In addition, price growth in extraction of crude oil and natural gas (15.2% yoy) and coal (25.9% yoy) significantly accelerated, driven by global price developments. Prices in production of coke and refined petroleum products also grew faster (26.1% yoy). Such developments, together with rising global prices for fertilizers, caused prices in the chemical industry to accelerate (up to 8.0% yoy).

Prices in supply of electricity, gas, steam and air-conditioned air also accelerated (to 23.4% yoy) on the back of rising world energy prices. In particular, in May "Naftogaz" NJSC raised tariffs on natural gas supply for industrial consumers by 5.2-5.5%.

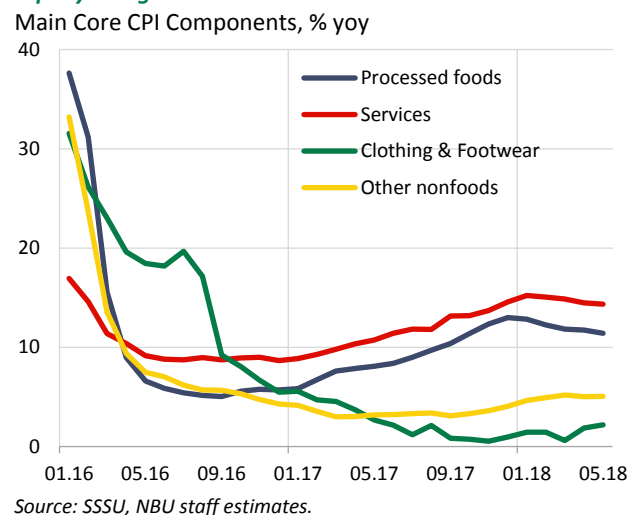
Meanwhile, the rate of growth in prices in metallurgy decreased (to 17.7% yoy), in particular due to lower prices for iron ore in previous periods.

Price growth in manufacture of foods, beverages and tobacco products also decelerated (to 10.0% yoy). Price growth in meat production slowed slightly (to 18.4% yoy) amid higher import supply of raw materials. Growth in prices for bakery and farinaceous products and in beverage production slowed (13.1% yoy and 16.5% yoy respectively). At the same time, prices in sugar production declined at a slower pace (to 20.2% yoy) amid expanding exports. Also, prices in production of dairy products rose at a slightly faster pace (13.7% yoy).

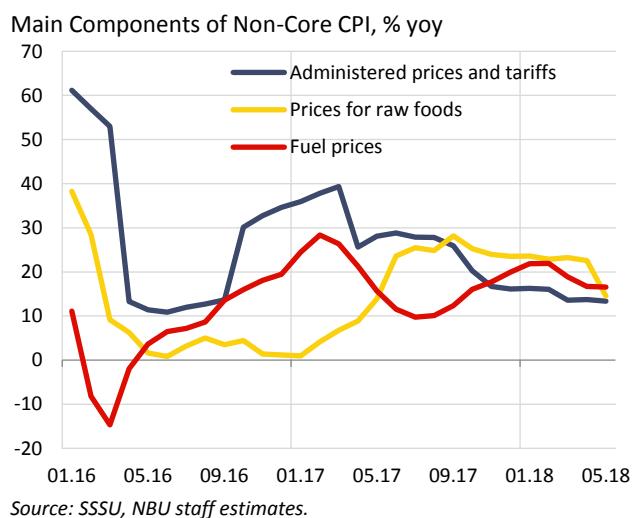
**In May 2018, headline and core inflation decelerated**



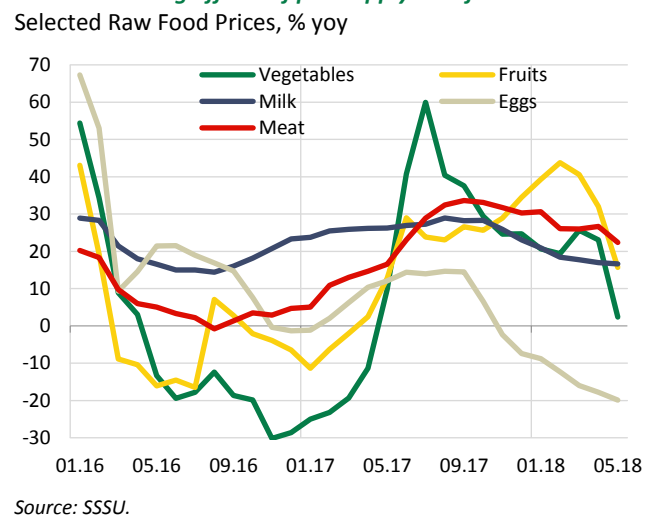
**Strengthening of the hryvnia effective exchange rate contributed to the deceleration in the core CPI, offsetting the rapidly rising consumer demand and increased costs**



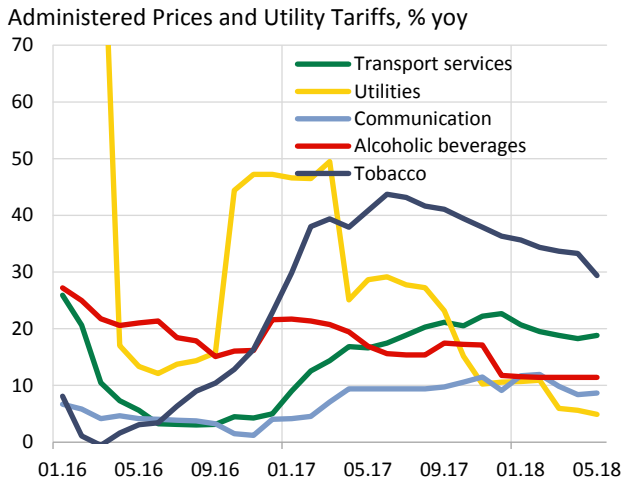
**A slowdown in headline inflation was mainly driven by raw food prices**



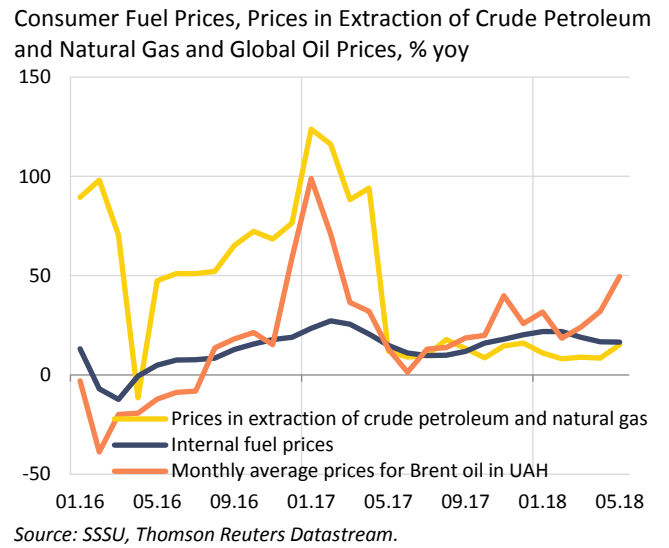
**Inflation for most raw food items considerably slowed down due to vanishing effects of past supply-side factors**



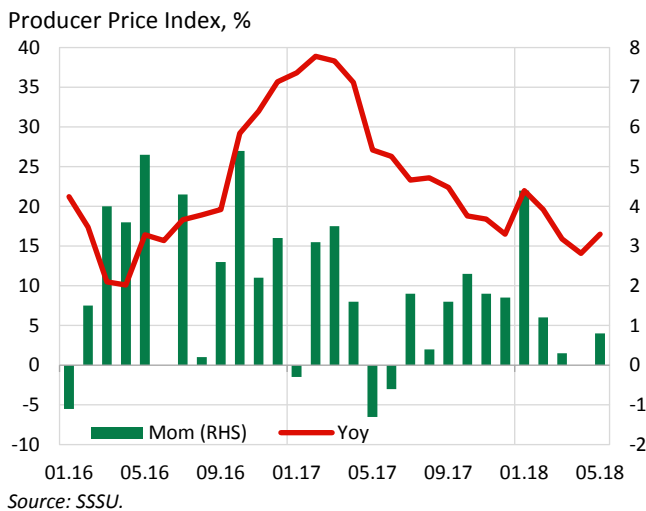
The rate of growth in administered prices decreased, in particular, due to the slowing prices for tobacco products and utilities



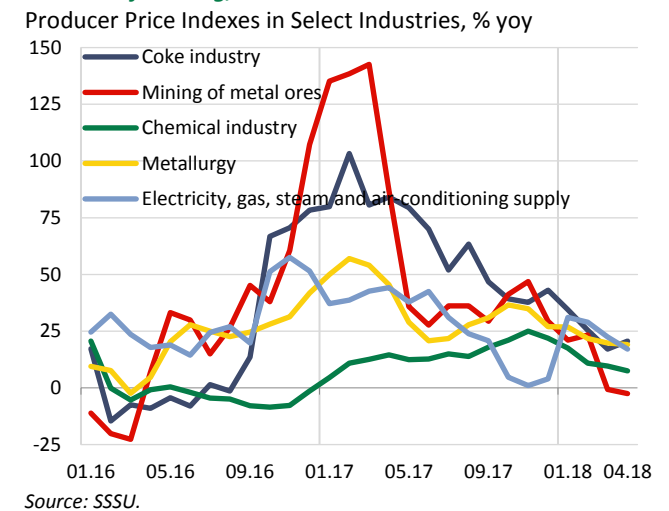
In May, fuel prices slowed down on the back of the benign FX market conditions. However, rising global oil prices somewhat restrained the slowdown



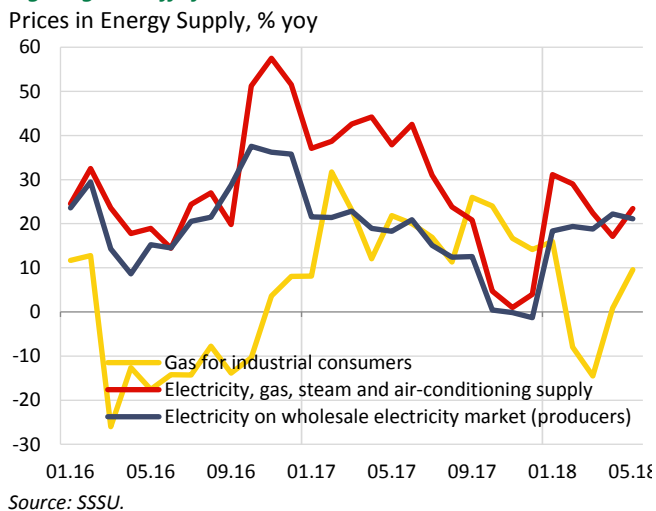
In May 2018, the producer price index accelerated...



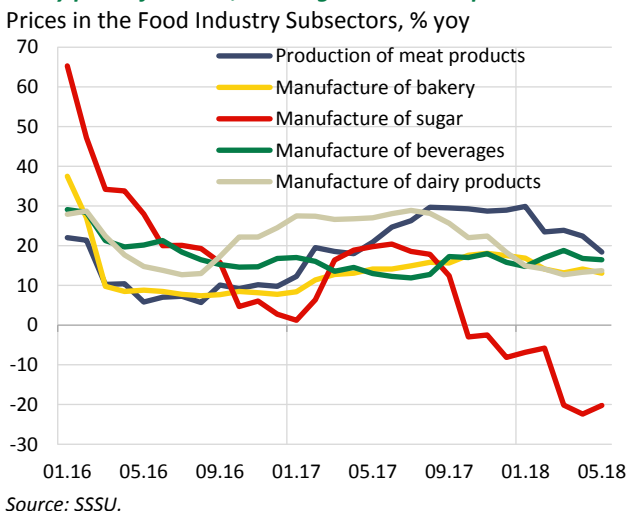
... due to the price upsurge in selected subindustries of mining and manufacturing, ...



... as well as in supply of energy and air-conditioning due to higher gas tariffs for industrial consumers



Price growth in food industry decelerated with the slowdown led by prices for meat, beverages and bread production



**CPI and PPI growth by components in 2016 - 2018**

	Share in CPI for 2018, %	2016	2017	% yoy					% mom May
				Jan	Feb	2018 Mar	Apr	May	
<b>CPI (NBU classification)</b>									
<b>Consumer Price Index</b>	<b>100.0</b>	<b>12.4</b>	<b>13.7</b>	<b>14.1</b>	<b>14.0</b>	<b>13.2</b>	<b>13.1</b>	<b>11.7</b>	<b>0.0</b>
<b>Core inflation</b>	<b>58.9</b>	<b>5.8</b>	<b>9.5</b>	<b>9.8</b>	<b>9.7</b>	<b>9.4</b>	<b>9.4</b>	<b>9.3</b>	<b>0.2</b>
<b>Non-core inflation *</b>	<b>41.1</b>	<b>17.5</b>	<b>19.4</b>	<b>19.8</b>	<b>19.4</b>	<b>17.9</b>	<b>17.5</b>	<b>14.1</b>	<b>-0.4</b>
Raw foods	18.6	1.2	23.5	23.6	22.9	23.3	22.6	14.5	-2.2
Administered prices and tariffs	18.5	34.6	16.1	16.2	16.1	13.6	13.7	13.3	1.1
Fuels	4.0	19.5	20.0	21.8	21.9	18.9	16.7	16.5	0.8

**CPI (State Statistics Service of Ukraine classification)**

<b>Food and non-alcohol</b>	<b>42.6</b>	<b>3.3</b>	<b>17.7</b>	<b>17.9</b>	<b>17.3</b>	<b>17.3</b>	<b>17.2</b>	<b>13.7</b>	<b>-0.7</b>
<b>Alcohol, tobacco</b>	<b>8.3</b>	<b>22.5</b>	<b>20.7</b>	<b>20.6</b>	<b>20.2</b>	<b>20.2</b>	<b>20.5</b>	<b>19.4</b>	<b>1.8</b>
<b>Clothing and footwear</b>	<b>5.6</b>	<b>5.5</b>	<b>0.9</b>	<b>1.4</b>	<b>1.4</b>	<b>0.5</b>	<b>1.7</b>	<b>2.4</b>	<b>-0.4</b>
<b>Housing, water, electricity, gas and other fuels incl.:</b>	<b>6.1</b>	<b>47.2</b>	<b>10.6</b>	<b>10.7</b>	<b>10.9</b>	<b>6.0</b>	<b>5.6</b>	<b>4.9</b>	<b>0.1</b>
Dwelling maintenance	0.3	11.5	47.5	52.7	52.1	48.1	41.6	37.2	1.2
Water supply	0.2	42.1	20.2	20.6	22.8	23.4	21.4	14.9	2.2
Hot water	0.2	82.9	0.9	0.9	0.9	0.9	0.9	-0.2	-1.1
Natural gas	1.7	42.0	1.2	1.2	1.2	1.2	1.2	0.3	0.0
Central heating	1.1	89.3	3.8	3.7	3.7	3.7	3.8	3.8	0.0
Electricity	1.0	60.0	28.1	28.1	28.1	0.0	0.0	0.0	0.0
<b>Transport</b>	<b>11.8</b>	<b>11.4</b>	<b>16.7</b>	<b>17.1</b>	<b>16.5</b>	<b>14.9</b>	<b>13.6</b>	<b>13.7</b>	<b>0.6</b>
<b>Communication</b>	<b>3.1</b>	<b>4.0</b>	<b>9.1</b>	<b>11.7</b>	<b>11.9</b>	<b>9.9</b>	<b>8.4</b>	<b>8.7</b>	<b>0.4</b>
<b>Education</b>	<b>1.5</b>	<b>13.7</b>	<b>14.9</b>	<b>15.3</b>	<b>15.3</b>	<b>15.3</b>	<b>15.3</b>	<b>15.2</b>	<b>0.0</b>

**PPI**

	Share in PPI for 2018, %**	2016	2017	% yoy					% mom May
				Jan	Feb	2018 Mar	Apr	May	
<b>Producer Price Index</b>	<b>100.0</b>	<b>35.7</b>	<b>16.5</b>	<b>22.0</b>	<b>19.6</b>	<b>15.9</b>	<b>14.1</b>	<b>16.5</b>	<b>0.8</b>
<b>Mining and quarrying</b>	<b>14.7</b>	<b>85.1</b>	<b>30.4</b>	<b>23.1</b>	<b>23.5</b>	<b>12.7</b>	<b>8.3</b>	<b>18.9</b>	<b>-0.9</b>
Manufacturing of coal	2.5	40.4	47.8	37.1	39.1	39.1	22.0	25.9	4.3
Extraction of crude petroleum and natural gas	5.1	76.5	16.1	11.1	8.2	8.9	8.4	15.2	3.5
Mining of metal ores	6.0	107.2	29.3	21.1	23.3	-0.7	-2.6	16.1	-7.0
<b>Manufacturing</b>	<b>65.7</b>	<b>22.6</b>	<b>18.5</b>	<b>18.0</b>	<b>15.2</b>	<b>13.7</b>	<b>13.9</b>	<b>13.6</b>	<b>0.3</b>
Manufacture of food products, beverages and tobacco products	21.2	16.2	12.5	11.9	10.9	10.3	10.7	10.0	0.1
Manufacture of coke, and refined petroleum products	3.9	61.7	43.0	34.4	25.4	17.1	20.6	26.1	3.6
Manufacture of chemicals and chemical products	2.8	-1.4	21.9	17.5	10.9	9.6	7.5	8.0	0.3
Manufacture of basic pharmaceutical products and pharmaceutical preparations	1.4	8.5	11.0	11.9	10.2	11.5	11.5	11.8	0.8
Manufacture of rubber and plastics products, and other non-metallic mineral products	5.1	9.5	12.5	13.8	11.7	11.8	11.9	11.9	0.6
Manufacture of basic metals and fabricated metal products, except machinery and equipment	18.4	41.8	26.9	26.8	21.7	19.7	19.1	17.7	-0.6
Manufacture of transport equipment	2.8	11.4	17.9	22.1	16.7	18.7	16.0	16.6	1.2
<b>Electricity, gas, steam and air-conditioning supply</b>	<b>19.6</b>	<b>51.5</b>	<b>4.0</b>	<b>31.1</b>	<b>29.0</b>	<b>22.4</b>	<b>17.1</b>	<b>23.4</b>	<b>3.1</b>

\* Revised NBU staff estimates based on the State Statistics Service of Ukraine data. The sum of contributions of CPI components may deviate from the total CPI through the use of dynamic weights according to the methodology of the SSSU and rounding.

\*\* The shares of PPI components are NBU staff estimates based on the SSSU data on volume of industrial production by type of activity for 2017.

*The Review is a translation of the original text in Ukrainian. In case of any discrepancies between the original document and its English translation, readers should consider the Ukrainian version of the Review as correct.*

**Terms and abbreviations:**

CPI – Consumer Price Index

PPI – Producer Price Index

NBU – National Bank of Ukraine

SSSU – State Statistics Service of Ukraine

yoy – in annual terms; year-on-year change

mom – in monthly terms; month-on-month change